

## § 1.338-1

## 26 CFR Ch. I (4-1-99 Edition)

- (1) Patents and similar property.
- (i) Scope.
- (ii) Specific allocation.
- (2) Internal Revenue Service authority.
- (h) Changes in old target's aggregate deemed sale price of assets.
  - (1) General rule.
  - (i) In general.
  - (ii) Redetermination of aggregate deemed sale price if the elective formula under section 338(h)(11) is used.
  - (iii) Redetermination of aggregate deemed sale price if the elective formula under section 338(h)(11) is not used.
  - (2) Procedure for transactions in which section 338(h)(10) is not elected.
  - (i) Income or loss included in new target's return.
  - (ii) Carryovers and carrybacks.
  - (A) Loss carryovers to new target taxable years.
  - (B) Loss carrybacks to taxable years of old target.
  - (C) Credit carryovers and carrybacks.
  - (3) Procedure for transactions in which section 338(h)(10) is elected.
  - (i) [Reserved.]
  - (j) Examples.

### *§ 1.338(h)(10)-1 Deemed asset sale and liquidation.*

- (a) Scope.
- (b) Nomenclature.
- (c) Definitions.
- (1) Section 338(h)(10) target.
- (2) S corporation shareholders.
- (3) Selling consolidated group.
- (4) Selling affiliate.
- (d) Section 338(h)(10) election.
- (1) In general.
- (2) Simultaneous joint election requirement.
- (3) Irrevocability.
- (4) Effect of invalid election.
- (e) Certain consequences of section 338(h)(10) election.
- (1) Old T.
- (2) Selling consolidated group, selling affiliate, or S corporation shareholders.
- (i) In general.
- (ii) Deemed liquidation of old T.
- (iii) Basis of stock not acquired.
- (iv) T stock sale.
- (v) Example.
- (3) Certain minority shareholders.
- (i) In general.
- (ii) T stock sale.
- (iii) T stock not acquired.
- (4) P.
- (5) New T.
- (6) Consolidated return of selling consolidated group.
- (f) Deemed sale price.
  - (1) General rule.
  - (2) Formula.
  - (3) Liabilities.
  - (4) Other relevant items.

- (5) Cross-reference.
- (g) Examples.
- (h) Inapplicability of provisions.

### *§ 1.338(i)-1 Effective dates.*

- (a) In general.
- (b) Elective retroactive application.
- (c) MADSP.
- (d) Deemed election.

[T.D. 8515, 59 FR 2960, Jan. 20, 1994, as amended by T.D. 8626, 60 FR 54944, Oct. 27, 1995; T.D. 8711, 62 FR 2268, Jan. 16, 1997; T.D. 8710, 62 FR 3459, Jan. 23, 1997]

## **§ 1.338-1 Elections under section 338.**

(a) *Scope.* This section prescribes rules relating to elections under section 338. Paragraphs (c)(6), (e), and (g) of this section do not apply to a target for which a section 338(h)(10) election is made.

(b) *Nomenclature.* For purposes of the regulations under section 338 (except as otherwise provided):

(1) T is a domestic corporation that has only one class of stock outstanding.

(2) P is a domestic corporation that purchases stock of T in a qualified stock purchase.

(3) The P group is an affiliated group of which P is a member.

(4) P1, P2, etc., are domestic corporations that are members of the P group.

(5) T1, T2, etc., are domestic corporations that are target affiliates of T. These corporations (T1, T2, etc.) have only one class of stock outstanding and may also be targets.

(6) S is a domestic corporation (unrelated to P and B) that owns T prior to the purchase of T by P. (S is referred to in cases in which it is appropriate to consider the effects of having all of the outstanding stock of T owned by a domestic corporation.)

(7) A, a U.S. resident or citizen, is an individual (unrelated to P and B) who owns T prior to the purchase of T by P. (A is referred to in cases in which it is appropriate to consider the effects of having all of the outstanding stock of T owned by an individual who is a U.S. resident or citizen. Ownership of T by A and ownership of T by S are mutually exclusive circumstances.)

(8) B, a U.S. resident or citizen, is an individual (unrelated to T, S, and A) who owns the stock of P.

(9) *F*, used as a prefix with the other terms in this paragraph (b), connotes foreign, rather than domestic, status. For example, FT is a foreign corporation (as defined in section 7701(a)(5)) and FA is an individual other than a U.S. citizen or resident.

(10) *CFC*, used as a prefix with the other terms in this paragraph (b) referring to a corporation, connotes a controlled foreign corporation (as defined in section 957, taking into account section 953(c)). A corporation identified with the prefix *F* may be a controlled foreign corporation. The prefix *CFC* is used when the corporation's status as a controlled foreign corporation is significant.

(c) *Definitions*. For purposes of the regulations under section 338 (except as otherwise provided):

(1) *Acquisition date*. The term *acquisition date* has the same meaning as in section 338(h)(2).

(2) *Affiliated group*. The term *affiliated group* has the same meaning as in section 338(h)(5). Corporations are affiliated on any day they are members of the same affiliated group with each other.

(3) *Common parent*. The term *common parent* has the same meaning as in section 1504.

(4) *Consistency period*. The *consistency period* is the period described in section 338(h)(4)(A) unless extended pursuant to § 1.338-4(j)(1).

(5) *Domestic corporation*. A *domestic corporation* is a corporation—

(i) That is domestic within the meaning of section 7701(a)(4) or that is treated as domestic for purposes of subtitle A of the Internal Revenue Code (e.g., to which an election under section 953(d) or 1504(d) applies); and

(ii) That is not a DISC, a corporation described in section 1248(e), or a corporation to which an election under section 936 applies.

(6) *Old target's final return*. *Old target's final return* is the income tax return of old target for the taxable year ending at the close of the acquisition date that includes the deemed sale of assets under section 338. If the disaffiliation rule of paragraph (e)(2)(i) of this section applies, target's *deemed sale return* is considered old target's final return.

(7) *Purchasing corporation*. The term *purchasing corporation* has the same meaning as in section 338(d)(1). Unless otherwise provided, any reference to the purchasing corporation is a reference to all members of the affiliated group of which the purchasing corporation is a member. See sections 338(h) (5) and (8).

(8) *Qualified stock purchase*. The term *qualified stock purchase* has the same meaning as in section 338(d)(3).

(9) *Related persons*. Two persons are related if stock in a corporation owned by one of the persons would be attributed under section 318(a) (other than section 318(a)(4)) to the other.

(10) *Section 338 election*. A *section 338 election* is an election to apply section 338(a) to target. A section 338 election may be made by filing a statement of section 338 election pursuant to § 1.338-1(d). The form on which this statement is filed is referred to in the regulations under section 338 as the *Form 8023*.

(11) *Section 338(h)(10) election*. A *section 338(h)(10) election* is an election to apply section 338(h)(10) to target. A section 338(h)(10) election may be made by making a joint election for target under § 1.338(h)(10)-1.

(12) *Selling group*. The *selling group* is the affiliated group (as defined in section 1504) that is eligible to file a consolidated return that includes target for the target's taxable period that includes the acquisition date and that does not have a target as common parent for the taxable year including the acquisition date.

(13) *Target; old target; new target*. *Target* is the target corporation as defined in section 338(d)(2). *Old target* refers to target for periods ending as of the close of the date of target's deemed sale of assets. *New target* refers to target for subsequent periods.

(14) *Target affiliate*. The term *target affiliate* has the same meaning as in section 338(h)(6) (applied without section 338(h)(6)(B)(i)). Thus, a corporation described in section 338(h)(6)(B)(i) is considered a target affiliate for all purposes of section 338. If a target affiliate is acquired in a qualified stock purchase, it is also a target.

(15) *12-month acquisition period*. The *12-month acquisition period* is the period

described in section 338(h)(1), unless extended pursuant to § 1.338-4(j)(2).

(d) *Time and manner of making election.* The purchasing corporation makes a section 338 election for target by filing a statement of section 338 election on Form 8023 in accordance with the instructions to the form. The section 338 election must be made not later than the 15th day of the 9th month beginning after the month in which the acquisition date occurs. A section 338 election is irrevocable.

(e) *Returns including tax liability from deemed sale—(1) In general.* Except as provided in paragraphs (e)(2) and (3) of this section, any tax liability resulting from the deemed sale of assets under section 338 is included in the final return of old target filed for old target's taxable year that ends at the close of the acquisition date. If old target is the common parent of an affiliated group, the final return may be a consolidated return (any such consolidated return must also include any tax liability from any deemed sales under section 338 by subsidiaries in the consolidated group that have the same acquisition date as old target and that are acquired by the purchasing corporation).

(2) *Old target's final taxable year otherwise included in consolidated return of selling group—(i) General rule.* If the selling group files a consolidated return for the period that includes the acquisition date, old target is disaffiliated from that group immediately before its deemed sale of assets under section 338 and must file a separate final return that includes only the items resulting from the deemed sale and the carryover items specified in paragraph (e)(2)(iii) of this section (deemed sale return). The deemed sale occurs at the close of the acquisition date and is the last transaction of old target. Any transactions of old target occurring on the acquisition date other than the deemed sale are included in the selling group's consolidated return. A deemed sale return includes a *combined return* as defined in paragraph (e)(4) of this section.

(ii) *Separate taxable year.* The deemed sale included in the deemed sale return under this paragraph (e)(2) occurs in a separate taxable year, except that old target's taxable year of the sale and

the consolidated year of the selling group that includes the acquisition date are treated as the same year for purposes of determining the number of years in a carryover or carryback period.

(iii) *Carryover and carryback of tax attributes.* Target's attributes may be carried over to, and carried back from, the deemed sale return under the rules applicable to a corporation that ceases to be a member of a consolidated group.

(iv) *Old target is a component member of purchasing corporation's controlled group.* For purposes of its deemed sale return, target is a component member of the controlled group of corporations including the purchasing corporation unless target is treated as an excluded member under section 1563(b)(2).

(3) *Old target an S corporation.* If target is an S corporation for the period that ends on the day before the acquisition date, old target must file a deemed sale return as a C corporation. For this purpose, the principles of paragraph (e)(2) of this section apply.

(4) *Combined deemed sale return—(i) General rule.* Under section 338(h)(15), a combined deemed sale return (combined return) may be filed for all targets from a single selling consolidated group (as defined in § 1.338(h)(10)-1(c)(3)) that are acquired by the purchasing corporation on the same acquisition date and that otherwise would be required to file separate deemed sale returns. The combined return must include all such targets. For example, T and T1 may be included in a combined return if—

(A) T and T1 are directly owned subsidiaries of S;

(B) S is the common parent of a consolidated group; and

(C) P makes qualified stock purchases of T and T1 on the same acquisition date.

(ii) *Gain and loss offsets.* Gains and losses recognized on the deemed sale of assets by targets included in a combined return are treated as the gains and losses of a single target. In addition, loss carryovers of a target that were not subject to the separate return limitation year restrictions (SRLY restrictions) of the consolidated return regulations while that target was a

member of the selling consolidated group may be applied without limitation to the gains of other targets included in the combined return. If, however, a target has loss carryovers that were subject to the SRLY restrictions while that target was a member of the selling consolidated group, the use of those losses in the combined return continues to be subject to those restrictions, applied in the same manner as if the combined return were a consolidated return. A similar rule applies, when appropriate, to other tax attributes.

(iii) *Procedure for filing a combined return.* A combined return is made by filing a single corporation income tax return in lieu of separate deemed sale returns for all targets required to be included in the combined return. The combined return reflects the deemed sales of all targets required to be included in the combined return. If the targets included in the combined return constitute a single affiliated group within the meaning of section 1504(a), the income tax return is signed by an officer of the common parent of that group. Otherwise, the return must be signed by an officer of each target included in the combined return. Rules similar to the rules in § 1.1502-75(j) apply for purposes of preparing the combined return. The combined return must include an attachment prominently identified as an "ELECTION TO FILE A COMBINED RETURN UNDER SECTION 338(h)(15)." The attachment must—

(A) Contain the name, address, and employer identification number of each target required to be included in the combined return;

(B) Contain the following declaration (or a substantially similar declaration): "EACH TARGET IDENTIFIED IN THIS ELECTION TO FILE A COMBINED RETURN CONSENTS TO THE FILING OF A COMBINED RETURN"; and

(C) For each target, be signed by a person who states under penalties of perjury that he or she is authorized to act on behalf of such target.

(iv) *Consequences of filing a combined return.* Each target included in a combined return is severally liable for any

tax associated with the combined return. See § 1.338-2(d)(1).

(5) *Deemed sale excluded from purchasing corporation's consolidated return.* Old target may not be considered a member of any affiliated group that includes the purchasing corporation with respect to the deemed sale of target assets under section 338.

(6) *Due date for old target's final return—*(i) *General rule.* Old target's final return is generally due on the 15th day of the third calendar month following the month in which the acquisition date occurs. See section 6072 (time for filing income tax returns).

(ii) *Application of § 1.1502-76(c)—*(A) *In general.* Section 1.1502-76(c) applies to old target's final return if old target was a member of a selling group that did not file consolidated returns for the taxable year of the common parent that precedes the year that includes old target's acquisition date. If the selling group has not filed a consolidated return that includes old target's taxable period that ends on the acquisition date, target may, on or before the final return due date (including extensions), either—

(1) File a deemed sale return on the assumption that the selling group will file the consolidated return; or

(2) File a return for so much of old target's taxable period as ends at the close of the acquisition date on the assumption that the consolidated return will not be filed.

(B) *Deemed extension.* For purposes of applying § 1.1502-76(c)(2), an extension of time to file old target's final return is considered to be in effect until the last date for making the election under section 338.

(C) *Erroneous filing of deemed sale return.* If, pursuant to this paragraph (e)(6)(ii), target files a deemed sale return but the selling group does not file a consolidated return, target must file a substituted return for old target not later than the due date (including extensions) for the return of the common parent with which old target would have been included in the consolidated return. The substituted return is for so much of old target's taxable year as ends at the close of the acquisition date. Under § 1.1502-76(c)(2), the deemed sale return is not considered a return

for purposes of section 6011 (relating to the general requirement of filing a return) if a substituted return must be filed.

(D) *Erroneous filing of return for regular tax year.* If, pursuant to this paragraph (e)(6)(ii), target files a return for so much of old target's regular taxable year as ends at the close of the acquisition date but the selling group files a consolidated return, target must file an amended return for old target not later than the due date (including extensions) for the selling group's consolidated return. (The amended return is a deemed sale return.)

(E) *Last date for payment of tax.* If either a substituted or amended final return of old target is filed pursuant to this paragraph (e)(6)(ii), the last date prescribed for payment of tax is the final return due date (as defined in paragraph (e)(6)(i) of this section).

(7) *Examples.* This paragraph (e) may be illustrated by the following examples:

*Example 1.* (a) S is the common parent of a consolidated group that includes T. The S group files calendar year consolidated returns. At the close of June 30 of Year 1, P makes a qualified stock purchase of T from S. P makes a section 338 election for T, and the deemed sale of T's assets occurs as of the close of T's acquisition date (June 30).

(b) T is considered disaffiliated for purposes of reporting the deemed sale. Accordingly, T is included in the S group's consolidated return through T's acquisition date except that the tax liability resulting from the deemed sale of assets is reported in a separate deemed sale return of T. Provided that T is not treated as an excluded member under section 1563(b)(2), T is a component member of P's controlled group for the taxable year represented by the deemed sale, and the taxable income bracket amounts available in calculating tax on the deemed sale return must be limited accordingly.

(c) If P purchased the stock of T at 10 a.m. on June 30 of Year 1, the results would be the same. See paragraph (e)(2)(i) of this section.

*Example 2.* The facts are the same as in *Example 1*, except that the S group does not file consolidated returns. T must file a separate return for its taxable year ending on June 30 of Year 1, which includes the deemed sale.

(f) *Waiver—(1) Certain additions to tax.* An addition to tax or additional amount (addition) under subchapter A of chapter 68 of the Internal Revenue Code arising on or before the last day for making the election under section

338, by reason of circumstances that would not exist but for an election under section 338, is waived if—

(i) Under the particular statute the addition is excusable upon a showing of reasonable cause; and

(ii) Corrective action is taken on or before the last day.

(2) *Notification.* The Service should be notified at the time of correction (e.g., by attaching a statement to a return that constitutes corrective action) that the waiver rule of this paragraph (f) is being asserted.

(3) *Elections or other actions required to be specified on a timely filed return—(i) In general.* If paragraph (f)(1) of this section applies or would apply if there was an underpayment, any election or other action that must be specified on a timely filed return for the taxable period covered by the late filed return described in paragraph (f)(1) of this section is considered timely if specified on a late-filed return filed on or before the last day for making the election under section 338.

(ii) *New target in purchasing corporation's consolidated return.* If new target is includible for its first taxable year in a consolidated return filed by the affiliated group of which the purchasing corporation is a member on or before the last day for making the election under section 338, any election or other action that must be specified in a timely filed return for new target's first taxable year (but which is not specified in the consolidated return) is considered timely if specified in an amended return filed on or before such last day, at the place where the consolidated return was filed.

(4) *Examples.* This paragraph (f) may be illustrated by the following examples:

*Example 1.* T is an unaffiliated corporation with a tax year ending March 31. At the close of September 20 of Year 1, P makes a qualified stock purchase of T. P does not join in filing a consolidated return. P makes a section 338 election for T on or before June 15 of Year 2, which causes T's taxable year to end as of the close of September 20 of Year 1. An income tax return for T's taxable period ending on September 20 of Year 1 was due on December 15 of Year 1. Additions to tax for failure to file a return and to pay tax shown on a return will not be imposed if T's return is filed and the tax paid on or before June 15 of

Year 2. (This waiver applies even if the acquisition date coincides with the last day of T's former taxable year, i.e., March 31 of Year 2.) Interest on any underpayment of tax for old T's short taxable year ending September 20 of Year 1 runs from December 15 of Year 1. A statement indicating that the waiver rule of § 1.338-1(f) is being asserted should be attached to T's return.

*Example 2.* Assume the same facts as in *Example 1*. Assume further that new T adopts the calendar year by filing, on or before June 15 of Year 2, its first return (for the period beginning on September 21 of Year 1 and ending on December 31 of Year 1) indicating that a calendar year is chosen. See § 1.338-2(d)(8). Any additions to tax or amounts described in this paragraph (f) which arise by reason of the late filing of a return for the period ending on December 31 of Year 1 are waived, because they are based on circumstances that would not exist but for the section 338 election. Notwithstanding this waiver, however, the return is still considered due March 15 of Year 2, and interest on any underpayment runs from that date.

*Example 3.* Assume the same facts as in *Example 2*, except that T's former taxable year ends on October 31. Although prior to the election old T had a return due on January 15 of Year 2 for its year ending October 31 of Year 1, that return need not be filed because a timely election under section 338 was made. Instead, old T must file a final return for the period ending on September 20 of Year 1, which is due on December 15 of Year 1.

(g) *Special rules for foreign corporations or DISCs—(1) Elections by certain foreign purchasing corporations—(i) General rule.* A qualifying foreign purchasing corporation is not required to file a statement of section 338 election for a qualifying foreign target before the earlier of 3 years after the acquisition date and the 180th day after the close of the purchasing corporation's taxable year within which a triggering event occurs.

(ii) *Qualifying foreign purchasing corporation.* A purchasing corporation is a *qualifying foreign purchasing corporation* only if, during the acquisition period of a qualifying foreign target, all the corporations in the purchasing corporation's affiliated group are foreign corporations that are not subject to United States tax.

(iii) *Qualifying foreign target.* A target is a *qualifying foreign target* only if target and its target affiliates are foreign corporations that, during target's acquisition period, are not subject to United States tax (and will not become

subject to United States tax during such period by reason of a section 338 election). A target affiliate is taken into account for purposes of the preceding sentence only if, during target's 12-month acquisition period, it is or becomes a member of the affiliated group that includes the purchasing corporation.

(iv) *Triggering event.* A triggering event occurs in the taxable year of the qualifying foreign purchasing corporation in which either that corporation or any corporation in its affiliated group becomes subject to United States tax.

(v) *Subject to United States tax.* For purposes of this paragraph (g)(1), a foreign corporation is considered *subject to United States tax*—

(A) For the taxable year for which that corporation is required under § 1.6012-2(g) (other than § 1.6012-2(g)(2)(i)(b)(2)) to file a United States income tax return; or

(B) For the period during which that corporation is a controlled foreign corporation, a passive foreign investment company for which an election under section 1295 is in effect, a foreign investment company, or a foreign corporation the stock ownership of which is described in section 552(a)(2).

(2) *Acquisition period.* For purposes of this paragraph (g), the term *acquisition period* means the period beginning on the first day of the 12-month acquisition period and ending on the acquisition date.

(3) *Statement of section 338 election may be filed by United States shareholders in certain cases.* The United States shareholders (as defined in section 951(b)) of a foreign purchasing corporation that is a controlled foreign corporation (as defined in section 957 (taking into account section 953(c))) may file a statement of section 338 election on behalf of the purchasing corporation if the purchasing corporation is not required under § 1.6012-2(g) (other than § 1.6012-2(g)(2)(i)(b)(2)) to file a United States income tax return for its taxable year that includes the acquisition date. Form 8023 must be filed as described in the form and its instructions and also must be attached to the Form 5471 (information return with respect to a foreign corporation) filed with respect to

the purchasing corporation by each United States shareholder for the purchasing corporation's taxable year that includes the acquisition date (or, if paragraph (g)(1)(i) of this section applies to the election, for the purchasing corporation's taxable year within which it becomes a controlled foreign corporation). The provisions of § 1.964-1(c) (including § 1.964-1(c)(7)) do not apply to an election made by the United States shareholders.

(4) *Notice requirement for U.S. persons holding stock in foreign target*—(i) *General rule.* If a target subject to a section 338 election was a controlled foreign corporation, a passive foreign investment company, or a foreign personal holding company at any time during the portion of its taxable year that ends on its acquisition date, the purchasing corporation must deliver written notice of the election (and a copy of Form 8023, its attachments and instructions) to—

(A) Each U.S. person (other than a member of the affiliated group of which the purchasing corporation is a member (the purchasing group member)) that, on the acquisition date of the foreign target, holds stock in the foreign target; and

(B) Each U.S. person (other than a purchasing group member) that sells stock in the foreign target to a purchasing group member during the foreign target's 12-month acquisition period.

(ii) *Limitation.* The notice requirement of this paragraph (g)(4) applies only where the section 338 election for the foreign target affects income, gain, loss, deduction, or credit of the U.S. person described in paragraph (g)(4)(i) of this section under section 551, 951, 1248, or 1293.

(iii) *Form of notice.* The notice to U.S. persons must be identified prominently as a notice of section 338 election and must—

(A) Contain the name, address, and employer identification number (if any) of, and the country (and, if relevant, the lesser political subdivision) under the laws of which is organized, the purchasing corporation and the relevant target (i.e., target the stock of which the particular U.S. person held or sold under the circumstances de-

scribed in paragraph (g)(4)(i) of this section);

(B) Identify those corporations as the purchasing corporation and the foreign target, respectively; and

(C) Contain the following declaration (or a substantially similar declaration): "THIS DOCUMENT SERVES AS NOTICE OF AN ELECTION UNDER SECTION 338 FOR THE ABOVE CITED FOREIGN TARGET THE STOCK OF WHICH YOU EITHER HELD OR SOLD UNDER THE CIRCUMSTANCES DESCRIBED IN TREASURY REGULATIONS § 1.338-1(g)(4). FOR POSSIBLE UNITED STATES FEDERAL INCOME TAX CONSEQUENCES UNDER SECTION 551, 951, 1248, OR 1293 OF THE INTERNAL REVENUE CODE OF 1986 THAT MAY APPLY TO YOU, SEE TREASURY REGULATIONS § 1.338-5(b). YOU MAY BE REQUIRED TO ATTACH THE INFORMATION ATTACHED TO THIS NOTICE TO CERTAIN RETURNS".

(iv) *Timing of notice.* The notice required by this paragraph (g)(4) must be delivered to the U.S. person on or before the later of the 120th day after the acquisition date of the particular target or the day on which Form 8023 is filed. If notice is delivered by United States mail, the date of the United States postmark is deemed to be the date of delivery.

(v) *Consequence of failure to comply.* A statement of section 338 election is not valid if timely notice is not given to one or more U.S. persons described in this paragraph (g)(4). If the form of notice fails to comply with all requirements of this paragraph (g)(4), the section 338 election is valid, but the waiver rule of paragraph (f)(1) of this section does not apply.

(vi) *Good faith effort to comply.* The purchasing corporation will be considered to have complied with this paragraph (g)(4), even though it failed to provide notice or provide timely notice to each person described in this paragraph (g)(4), if the Commissioner determines that the purchasing corporation made a good faith effort to identify and provide timely notice to those U.S. persons.

[T.D. 8515, 59 FR 2963, Jan. 20, 1994]